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Winston Hickox, Chair
Dr. Lawrence Goulder, Vice Chair
AB 32 Market Advisory Committee
c/o California Environmental Protection Agency
1001 I Street, 15th Floor
Sacramento, CA 95814

**SEMPRA ENERGY COMMENTS ON THE MARKET ADVISORY COMMITTEE RECOMMENDATIONS FOR DESIGNING A GREENHOUSE GAS CAP-AND-TRADE SYSTEM FOR CALIFORNIA**

Dear Dr. Hickox and Market Advisory Committee Members:

Sempra Energy appreciates the opportunity to comment on the California Market Advisory Committee's (CMAC) draft report - *Recommendations for designing a Greenhouse Gas Cap-and-Trade System for California* (the draft report). Based in San Diego, Sempra Energy is a Fortune 500 energy services holding company whose subsidiaries provide electricity, natural gas, and value-added products and services to more than 29 million customers worldwide.

The Global Warming Solutions Act of 2006 (AB 32) requires California to reduce the statewide greenhouse gas inventory to 1990 levels by 2020. Sempra Energy supports this goal and is committed to working with California policymakers to successfully implement AB 32. To achieve the legislation's ambitious goal, policymakers must critically examine a range of potential programs and measures, and carefully consider the impacts these may have across the economy. First among these considerations must be the cost of the program to all Californians, in particular, the cost of delivering essential services such as electricity and natural gas.

Sempra supports a market-based GHG cap-and-trade emissions program for California that includes as many sectors of the economy as possible. The program at a minimum should provide for the fair and equitable allocation of burden; promote the broad use of offset credits; contain safety valve provisions; and above all, be designed to control costs. We commend the CMAC in its development of the draft report which embraces many of these principles, and provide the following additional comments.

**Support of Market-Based Cap-and-Trade Emission Programs**
Sempra supports the CMAC's recommendation for a market-based cap-and-trade emission reduction program. These programs have been demonstrated to lower regulatory compliance costs and promote new technologies. A well designed (and well implemented) market program will encourage entities and/or individuals to engage in pollution control efforts that are in their own interests and

collectively meet policy goals. By contrast, “command-and-control” regulations provide less flexibility with regard to how entities achieve their environmental goals. Such regulations tend to force entities to take on a pollution-control burden for their particular circumstance without regard to less expensive alternatives. With little or no financial incentive for businesses to exceed their control targets, firms are not encouraged to develop new ideas and technologies. Therefore, to achieve the state’s ambitious emission reduction goals, stimulate innovation and new technology, address market failures, and control program costs, the state must utilize market programs in preference to command and control approaches.

**Program Scope**

Sempra Energy supports an economy-wide $CO^2$ emissions market for California at the outset of the program in lieu of the CMAC recommendation for a phased-in approach. A broad based program at the onset provides much needed liquidity and regulatory certainty for all market participants. As the CMAC report notes on page 35, the phased-in approach creates regulatory uncertainty as to when and whether transportation and other sectors -- which account for more than 50% of the state’s GHG inventory -- will be included, and to what degree.[1] If a phased-in approach is adopted, it will create uncertainty that would preclude or dampen investment and technology development, in both the covered sector and sectors that may be included in the future.

Further, the CMAC recommendation that the 2020 emissions cap be set equal to “total allowable emissions under the Global Warming Solutions Act minus projected emissions from sources and sectors not covered by the cap-and-trade program,” implies the burden of the capped sector can be changed (increased) should the non-capped sectors fail to produce their projected reductions. Such an outcome would be unacceptable as it inequitably allocates the GHG reduction burden to a minimal universe of participants. All sectors must do their fair share. To avoid these undesired consequences, we recommend establishing an economy-wide program at the outset.

**Electric Sector “First Seller Approach”**

Sempra remains flexible on program design for the electric sector. Again, our primary concern is that any program minimizes costs to our ratepayers and maximizes benefits.

We are currently evaluating the details of the first seller approach to fully identify the costs, benefits, and legal issues. Clearly, the merits of both a load-based approach and a first seller-based approach need to be fully analyzed so the state can implement a program design that achieves all the stated objectives of AB 32. We will continue to work with other program participants and the state in developing the best and lowest cost solution.

**Distribution of Allocations**

Sempra is studying the CMAC’s conclusions regarding auctions versus allocations in the context of a regime that would impose emission reduction responsibilities under a “first seller” approach to fully understand the implications of such a proposal. We support the recommendation that the state examine the micro-economic impacts of any distribution proposal and support benchmarking sector participants to encourage early action.

[1] Appendix C

**Offsets and Linkages**
Sempra supports CMAC's recommendations that the program include a broad range of verifiable offsets with no quantitative limits. Additionally, we support CMAC's recommendation to link California's program with other regional, national, and international GHG programs. These policies recognize the GHG reduction is a global effort and it increases the likelihood of other states and countries adopting similar policies. The CMAC is correct in seeking global solutions to a global problem.

**Safety Valve**
In contrast to the CMAC recommendation, Sempra supports the inclusion of a safety valve, or program off-ramp. Understandably, these policy instruments have some effect on investment and market dynamics; however, the consequence of a delay in reducing state-wide GHGs is far less severe than a near-term economic melt down. We strongly recommend the CMAC consider alternatives that provide relief under program duress such as limited borrowing from future allocations and alternative compliance fees that can be directed into a climate mitigation trust.

Yours sincerely,

CAROLYN MCINTYRE
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